

Oil and Gas Bond Adequacy Review Action Plan
Montana/Dakotas
February, 2007

Purpose: Washington Office (WO) Instruction Memorandum (IM) No. 2006-206, Oil and Gas Bond Adequacy Review (Attachment 1), requires each State Office administering an oil and gas program to establish an action plan with a goal that operators on Federal oil and gas leases are reviewed for risk assessment and bond adequacy. The goal of this plan is to develop a process to ensure review of operations on Federal oil and gas leases and include steps to increase bond amounts when it is determined necessary.

Background: The regulations under 43 CFR 3104 require that the lessee, operating rights owner, or operator provide bond coverage prior to surface disturbing activities and to maintain adequate bond coverage during the operation period of a lease. The Authorized Officer (AO) may require an increase in the amount of any bond whenever it is determined that the operator poses a risk. Risk factors include, but are not limited to, a history of previous violations, a notice from the Minerals Management Service that uncollected royalties are due, or when the total cost of plugging existing wells and reclaiming lands exceeds the present bond amount based on the estimates determined by the AO and the lessees' economic condition warrant concern about their ability to meet the cost of plugging and reclamation.

The Montana/Dakotas organization has taken an active role in reviewing bond adequacy for many years. Numerous IMs have been issued which provide guidance on the review of shut-in and temporarily abandoned wells and the review of adequate bond coverage. Numerous bonds have been increased when risk has been identified. The review of bond adequacy in conjunction with the review of idle wells has been successful as there are no orphan wells in Montana/Dakotas. Policy and guidance have been in place for many years and are still applicable.

Action Plan: Offices will continue to review bonding and idle wells in accordance with existing guidance. Offices will also incorporate and follow the Bond Adequacy Review Process Description provided as an attachment to WO IM No. 2006-206. Bond adequacy reviews should be performed when any of the following actions occur:

1. The record title is assigned.
2. Operating rights are transferred.
3. A notification of change of operator.
4. The AO performs an Idle/Inactive well liability review.
5. The AO determines that the operator poses a risk (for example, operator compliance history, current level of plugging and surface reclamation liabilities, etc.).
6. An operator requests that a bond be released.
7. When the AO periodically reviews operating leases.

Responsibilities for bond review and bond increases are shared between the Montana State Office (MSO) Adjudication Section and the Field Offices/Stations (FOs). If a determination is made at the Field Office or Field Station that a bond should be increased, the process described in Part XIII of BLM Handbook 3104-1, Fluid Minerals Bond Processing User Guide, should be followed.

1. Roles and responsibilities for bond adequacy reviews

The Fluids Adjudication Section is responsible for bond adequacy reviews in certain situations. Bond adequacy reviews should be initiated when any of the following actions occur:

- The record title is assigned
- Operating rights are transferred

The process described in a memorandum to the Fluids Adjudication Section from the Chief, Fluids Adjudication Section dated March 20, 2001 (Attachment 2), is still applicable and should be followed. The reviews initiated by the Fluids Adjudication Section may require input from the FOs.

The Reservoir Management and Operations (RM&O) Section is responsible for ensuring a bond review prior to approval of a successor operator for unit operations. The reviews initiated by the RM&O Section will require input from the FOs.

The Miles City Field Office, North Dakota Field Office, and the Great Falls Oil and Gas Field Station are also responsible for bond adequacy reviews in certain situations. Bond adequacy reviews should be performed when any of the following actions occur:

- A notification of change of operator
- The AO performs an idle/inactive well liability review
- The AO determines that the operator poses a risk
- An operator requests that a bond be released
- When the AO periodically reviews operating leases

Idle/inactive well liability reviews should follow the procedures identified in the Montana/Dakotas Oil and Gas Idle Well Liability Action Plan dated July, 2001 (Attachment 3). With the spike in oil and gas prices within the last year, many idle wells should have been returned to production. Reviews should ensure that adequate justification is provided by the operators for wells that were not returned to production. Bond reviews should be performed in conjunction with the idle well reviews.

Special emphasis should be placed on reviewing wells that have been idle for longer than five years; especially those that are not within secondary recovery units. Wells that have been idle for longer than five years are specifically identified in the Idle Well Progress Report (WRT.12) generated in the Automated Minerals Support System (AFMSS) and

are in turn specifically identified in the Idle Well Progress Report submitted to the Washington Office in accordance with WO IM No. 2001-147. Wells that remain idle for longer than five years tend to pose a greater risk of becoming orphaned. Therefore, review of these wells should receive increased attention. Idle well reviews should be documented utilizing the Idle Well Review Screen (GLB.107), and bond reviews should be documented utilizing the Bond Review Screen (GLB.109) in AFMSS.

Emphasis should also be placed on ensuring timely and proper surface reclamation of plugged and abandoned wells. This allows for timely bond review when an operator requests that a bond be released, as well as fulfilling an important goal of the oil and gas program.

The MSO Branch of Fluid Minerals is responsible for providing policy direction and oversight of the bond adequacy review process.

2. Staff training and training assistance requirements

All of the individuals involved with the bond review process are experienced oil and gas personnel with the possible exception of the vacant petroleum engineer position in Miles City. Therefore, no formal staff training is necessary. Training of the new petroleum engineer can be accomplished by the current Miles City staff.

3. Impacts on other priority oil and gas workload

Implementation of this action plan should have a minimal impact on other oil and gas workloads since bond adequacy reviews are not new and have been a priority for many years.

4. State Office program oversight

The MSO Branch of Fluid Minerals will continue to conduct program oversight. Oversight will be conducted using the Idle Well Progress Report (WRT.12) and the Bonds Reviewed Report (GLB.102) in AFMSS. These reports are generated from the data entered by the FOs. Detailed program reviews will be conducted in the FOs if deemed necessary.

5. Previous accomplishments

Attached is a table (Attachment 4) showing previous bond increases on active bonds.

4 Attachments

- 1-WO IM No. 2006-206 (5 pp in its entirety)
- 2-Fluids Adjudication Section Process dated 3/20/01 (2 pp)
- 3-MT/DK O&G Idle Well Action Plan dated July 2001 (3 pp)
- 4-Bond Increases as of 2/06/07 (1 pg)

UNITED STATES DEPARTMENT OF THE INTERIOR
BUREAU OF LAND MANAGEMENT
WASHINGTON, D.C. 20240

August 3, 2006

In Reply Refer To:
3100 (310) P

EMS TRANSMISSION 08/08/2006
Instruction Memorandum No. 2006-206
Expires: 09/30/2007

To: All State Directors
From: Assistant Director, Minerals, Realty and Resource Protection
Subject: Oil and Gas Bond Adequacy Reviews

Program Area: Federal Oil and Gas Lease Operations and Bonding

Purpose: To reiterate regulatory and policy bonding requirements for oil and gas operations on Federal lands, including split estate lands, and on private lands.

Policy/Action: Each State Office (SO) administering an oil and gas program shall establish an action plan with a goal that operators on Federal oil and gas leases are reviewed for risk assessment and bond adequacy. The goal of the action plan is to develop a process to ensure review of operations on Federal oil and gas leases and include steps to increase bond amounts when it is determined necessary. When a review determines that an operator has an increase in activities, or when record title or operating rights are transferred and the transferor is the bonded party and is transferring all of its lease interests, or we are notified of a change of operator, the authorized officer (AO) will determine whether existing bonding is adequate.

The bond may be increased to any level specified by the AO, although the bond amount should not be increased solely on the number of wells on the lease. In no circumstance shall the bond amount exceed the total of the estimated cost of plugging and reclamation, the amount of uncollected royalties due, plus the amount of monies owed to the lessor due to previous violations remaining outstanding. If an operator's bond coverage is

Attachment 1-1

determined inadequate, the bonded party will be contacted and requested to increase its bonding or negotiate a plan to reduce plugging obligations and/or conduct reclamation work.

Additionally, the bond may be decreased if the Federal liability on the bond is reduced. This may occur when plugging and reclamation activities are performed on a lease or leases while some operational liabilities still remain under the bond. In other instances, State or other local jurisdictions may require new or increased bonding for liabilities already covered by the Federal bond. If these other jurisdictional bonds may be used to pay for Federal liabilities covered by our bond in case of operator default, then these bonds may be considered in reducing the Federal bond amount (but not below the regulatory minimum). The AO should take into account all liabilities secured by such bonds held by other governments in determining whether it is reasonable to reduce the Federal bond coverage in reliance on these bonds.

It is important that idle and inactive wells be reviewed and that continuous reclamation monitoring be conducted to identify potential problems and liabilities and to assess adequacy of existing bond amounts. Attachment 1 contains standard business process descriptions for bond adequacy reviews.

This memorandum is not intended to force across-the-board increases for all bonds. Upon your analysis, however, there are likely situations where a bond increase should be pursued. The judgment and field experience of your staff is paramount in making these determinations. We are mindful of the need to maintain an acceptable risk level, yet not to place an undue burden on industry.

Implementation of this policy and its progress will initially be evaluated during FY 2007.

Policy Clarification: The AO has the authority to require an increase to an existing statewide or nationwide bond, as well as an individual lease bond, to cover a specific liability on one or several Federal leases. Liabilities may include produced water impoundment structures, wells with significant liabilities, surface production facilities, or other surface uses with significant reclamation liabilities. This type of bond increase can be accomplished via a bond rider that is reserved solely for the liability specified, so that other demands on the statewide or nationwide bond could not draw on that increased amount of the bond.

The AO also has the authority to require bonding for reclamation of off-lease lands or surface waters that may be adversely affected by operations necessary on the leasehold. Examples of off-lease liability could include disposal pits, on-channel reservoirs or produced water impoundments constructed on private lands for use by one or more Federal leases. Bonding for these types of off-lease liabilities can be covered by a bond rider attached to a lease, a statewide or a nationwide oil and gas bond and should specify the specific off-lease liability to be covered. The AO must take into account the

existence of any other bond covering these off-lease liabilities required by BLM for example, a 2805 right-of-way bond, the State or other jurisdiction, in order to prevent duplication of bond coverage.

Timeframe: The guidance contained in this Instruction Memorandum is effective immediately.

Background: Task 7 of the National Energy Policy Implementation Plan requires the Bureau of Land Management (BLM) to explore improvements related to liability and reclamation of Federal oil and gas leases. The regulations under *43 CFR 3104-Bonds*, require that the lessee, operating rights owner, or operator provide bond coverage prior to surface disturbing activities and to maintain adequate bond coverage during the operational period of a lease. The AO may require an increase in the amount of any bond whenever it is determined that the operator poses a risk. Risk factors include, but are not limited to, a history of previous violations, a notice from the Minerals Management Service that uncollected royalties are due, or when the total cost of plugging existing wells and reclaiming lands exceeds the present bond amount based on the estimates determined by the AO and the lessees' economic condition warrant concern about their ability to meet the cost of plugging and reclamation.

Budget Impact: Some additional resources to perform an increased level of operator, lease operations and bond reviews may be required.

Regulation/Manual/Handbook Sections Affected: Regulations at 43 CFR 3104, 3106.6 and 3163.3-1, and Handbooks 3104-1 and 3106-1.

Coordination: BLM Washington, State and Field Office Staff, and the Solicitor's Office.

Contact: If you have any questions about this guidance, please contact Tim Spisak at (202) 452-5061.

Signed by:
Thomas P. Lonnie
Assistant Director
Minerals, Realty and Resource
Protection

Authenticated by:
Robert M. Williams
Division of IRM Governance, WO-560

1 Attachment

1- Bond Adequacy Review Process Description (2pp)

Attachment 1-3

Bond Adequacy Review Process Description

A. Process Scope.

Bond adequacy reviews should be performed when any of the following actions occur.

1. The record title is assigned (as workload permits).
2. Operating rights are transferred (as workload permits).
3. A notification of change of operator (as workload permits).
4. The AO performs an Idle/Inactive well liability review.
5. The AO determines that the operator poses a risk (for example, operator compliance history, current level of plugging and surface reclamation liabilities, etc.).
6. An operator requests that a bond be released.
7. When the AO periodically reviews operating leases.

B. The BLM field office determines the amount of well plugging and surface reclamation liability using cost indices.

If an increase in bonding is determined necessary in accordance with regulation (43 CFR 3104.5) and policy, the following actions will be performed.

1. Determine the well plugging and abandonment liability cost.
2. Determine the surface reclamation costs including pit closures, removal of equipment, and road reclamation.

C. The BLM determines an adequate level of bond coverage.

1. Bond amounts as stated in 43 CFR, Subpart 3104 are the minimum acceptable bond amounts.
2. Additional bond coverage cannot exceed the total cost of:
 - a. Estimated well plugging and surface reclamation,
 - b. Uncollected royalties, and
 - c. Monies owed for previous violations that remain payable.
3. The increase in bond amount may be to any level specified by the AO (but cannot exceed the limits as described above). The AO must be mindful to strike a balance between acceptable risk and an undue burden on the operator (such as removing an operator's limited operating capital earmarked for future liability reduction).
4. The BLM should observe associated state oil and gas bonding, especially when a state oil and gas conservation program provides funds for operations on Federal lands.
5. Existing bond amounts may be maintained in cases where an agreement is reached with the operator to reduce well plugging and surface reclamation responsibilities. The agreement should specify a plan of action to be performed in an acceptable timeframe.
6. If the bond amount is considered adequate, no action is required to increase the bond. The BLM may still require the operator to submit and follow through with a plan of action to ensure compliance with the lease terms and regulatory requirements.

D. Bond adjudicators render a decision concerning the adequacy of an existing bond amount.

1. If the field office bond increase recommendation is tenable, and the existing bond amount is verified inadequate, the operator (or lease interest holders, as appropriate) is issued a demand to raise the bond to a specified amount.
2. An operator (lease interest holders) may appeal the State Office decision to increase the bond.
3. The operator may comply by either filing an additional bond or attaching a rider to an existing lease, statement or nationwide bond



United States Department of the Interior



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Central Adjudication File (Bonds)
(922KJ)

March 20, 2001

Memorandum

To: Fluids Adjudication Section

From: Chief, Fluids Adjudication Section

Subject: Policy for Bond Review during Processing of Assignments
and Transfers

The purpose of this memorandum is to confirm our existing policy for ensuring adequate bond coverage prior to approving transfers which include record title assignments and operating rights transfers. This guidance changes our former procedures for leases where the existing bond is maintained by a Unit Operator.

Review for Bonding

For all incoming record title assignments and operating rights transfers filed on leases with an unplugged well(s), a review is completed by the Examiner to determine the bond that is covering outstanding lease obligations. This determination is made from retrieving and verifying information in LR2000, AFMSS, individual well records and the official lease file.

Bonded Parties Transferring All of Their Interest

If the bonded party is assigning **all** of its interest to another party, we will prepare a notice to the parties to the transfer requesting confirmation regarding who will provide bond coverage for the obligations following approval of the transfer. A sample notice is attached (Attachment 1). This procedure is in line with the Board of Land Appeal's ruling in Devon Energy Corp., 145 IBLA 136 (1998), copy attached. In Devon, the Board emphasizes that the BLM does not approve lease operator changes and cannot therefore hold an operator responsible for future lease obligations after approval of a transfer conveying the operator's lease interest to another party.

Attachment 2-1

Bonded Parties Transferring Only Part of Their Interest

If the bonded party is transferring only **part** of its interest away, we can proceed with approval of the transfer without requesting bond clarification.

Bonding Provided by Communitization and Unit Agreement Operators

For leases that are committed to agreements, if the bond coverage is maintained by the Agreement Operator, the transfer may be approved. It is not necessary to follow our prior procedures of requesting successor operator forms with proper bonding or confirmation that the existing operator will continue to maintain bond coverage for the lease. Bonding for Operators of unit and communitization agreements is handled differently because we **approve operators**. The approved operator is responsible and their bond coverage is maintained until a successor operator with appropriate bonding is filed and approved by the BLM.

Bonding Provided by Operators on the Ground/Not a Party to the Transfer

If the bond is maintained by the Operator and that Operator is not a transferor on the transfer document, you may proceed with approval of the transfer.

/s/ Karen L. Johnson

Karen L. Johnson, Chief
Fluids Adjudication Section

2 Attachments

- 1-Sample Notice
- 2-Copy of 145 IBLA 136 (1998)

Oil and Gas Idle Well Liability Action Plan
Montana/Dakotas
July, 2001

Purpose: Washington Office Instruction Memorandum (IM) 2001-147, Oil and Gas Idle Well Liability Action Plan Submission and Accomplishment Reporting Requirements, requires each State administering an oil and gas program to establish a plan that outlines procedures to combat idle wells that may become orphan wells. The IM also requires submission of the Idle Well Progress Report. This plan will ensure that the affected Montana/Dakotas offices continue efforts to reduce the number of idle wells.

Background: An idle well is defined as a well that has been shut-in or temporarily abandoned for 12 consecutive months or longer. Idle wells are considered a potential risk to the Federal Government. for the plugging and reclamation costs of the well. Therefore, offices must review the idle wells to ensure that every well without a viable future use is properly plugged and abandoned.

The Montana/Dakotas has taken an active role in reducing the number of idle wells since 1990. Consequently, we do not have any orphan wells. Numerous Instruction Memorandums have been issued which provide guidance on the review of shut-in and temporarily abandoned wells and the review of adequate bond coverage. The most recent IM, MT-2001-025 (Attachment 1), re-emphasized the review of idle wells. This IM included past guidance which is still applicable. Our fiscal year 2000 annual work plan directives (Attachment 2) instructed the offices to continue to work with their operators to reduce the number of temporarily abandoned and shut-in wells.

Action Plan: Offices will continue to review idle wells and bonding in accordance with the existing guidance. The well definitions, general process descriptions, and reporting requirements for the Management Information System outlined in WO IM No. 2001-147 (Attachment 3) will be followed. Attached (Attachment 4) is the initial Idle Well Progress Report. Following are the specific items required by the WO IM:

1. Roles and responsibilities for idle well and bond adequacy reviews.

The Great Falls Oil and Gas Field Station (GFFS), Miles City Field Office (MCFO), and North Dakota Field Office (NDFO) are responsible for review of idle wells and bond reviews. Bond reviews are to be conducted in conjunction with the idle well reviews. The Montana State Office (MSO) Fluids Adjudication Section is also responsible for bond reviews. These reviews will be conducted in accordance with the guidance provided by a memorandum (Attachment 5) dated March 20, 2001.

The MSO Branch of Fluid Minerals is responsible for providing policy direction and oversight of the idle well and bond adequacy reviews.

2. Summary and adequacy assessment of State's idle well inventory and workload by office.

	GFFS	MCFO	NDFO
Shut-in Idle Wells	256	86	52
Temporarily Abandoned Idle Wells	118	143	43

Many of the idle wells are located within secondary recovery units. These wells may have future uses as the production continues and the secondary recovery process is evaluated.

3. Planned Idle well and bond actions for FY2002 and FY2003.

Offices will continue to reviews idle wells and bonds in accordance with the existing guidance previously mentioned. The number idle wells should be reduced in the next two years provided oil and gas prices do not drop significantly.

4. Staff training and training assistance requirements.

With the exception of a new engineer in the GFFS, all of the individuals involved with the idle well review are experienced oil and gas personnel. Therefore, no formal staff training is anticipated. The new engineer will require some training and time to become familiar with the idle well program.

5. Required or allocated work months/funding needs for positions, travel, training, equipment, software, etc., for FY2002 through FY2003.

Approximately \$50,000 will be needed in each of the next two fiscal years to continue our idle well reviews. This amount will cover the work month costs for the individuals involved in the reviews. It will also cover travel costs associated with program oversight. No additional costs are anticipated at this time.

6. State Office program oversight (quality assurance/quality control plans).

The MSO will continue to conduct program oversight. This will involve review and analysis of the number of idle wells being reported. It will also involve field office visits for program reviews. A review was completed in the MCFO in FY2000. A review is scheduled for the NDFO this fiscal year. Reviews in future years will be conducted as determined by an analysis of the reported data. It is anticipated that at least one office will be reviewed each year.

7. Impacts on other workload such as leasing actions, permit review and approvals, inspection and enforcement, etc., to establish a minimum level idle well program.

The idle well program should have a minimal impact on other workloads with the exception of the MCFO. Assuming there is no significant increase in activity, the current staff in the NDFO and the GFFS (with the new engineer) should be able to handle the workload associated with the idle well program. In the MCFO, where coalbed methane development is expected to boom in the next few years, permit reviews could be impacted. However, it is anticipated that additional personnel will be added to handle the coalbed methane workload. If the additional personnel are added to handle the coalbed methane work, impacts on other workloads should be minimal.

8. Previous accomplishments.

Attached are tables (Attachments 6 and 7) showing historical statistics on shut-in and temporarily abandoned wells. Also attached is a table (Attachment 8) showing bond increases that were required due to the number of idle wells.

**BOND INCREASES ON
ACTIVE BONDS AS OF 3/16/06
MONTANA STATE OFFICE**

DATE OF ACTION	BONDED PARTY	BLM BOND NUMBER	BOND AMOUNT	REASON FOR BOND INCREASE
8/25/1997	Carrell Oil Company	MT0929	\$40,000 (Increased from \$25,000)	Amount determined by FO for well liabilities
4/20/2000	Titan Oil, Inc.	MT 1029	\$50,000 LIMITED TO 7 WELLS IN MT	Risk Operator with Noncompliance History
6/10/2000	EnCana Energy Resources Inc.	MT1009	\$250,000 (Increased from \$150,000)	New Operator/Substantial # of shut-in/TA wells
6/12/2000	Pride Energy Company	MT1002	\$75,000 (Increased from \$50,000)	Bond was for \$50,000 for two units of coverage for ND and WY. Wyoming requested increased coverage for Wyoming liabilities
11/29/2000	Encore Operating LP	MT1000	\$450,000 (Increased from \$300,000)	New Operator/Substantial # of shut-in/TA wells
8/28/2001 4/02/2002	J J Bunkirt Oil & Gas Corp.	MT1083	\$40,000 (Increased from \$10,000) Reduced to \$30,000	New Operator with full bonding for plugging costs/one well
6/12/2002	Solenex Inc. MTM 53323 Sidney Longwell owns Solenex	MT1104	Increase requested from \$10,000 to \$105,000 when APD approved	Amount determined by FO for reclamation costs/environmentally sensitive well proposal(FINA well) Solenex is new operator.
7/02/2004	Omimex Canada Ltd.	MTB000052	Increase Requested from \$150,000 to \$229,000	New Operator/Substantial # of shut-in/TA wells
11/16/2004	Robert Hawkins Inc.	MTB000082	\$25,000 (Increased from \$10,000)	Amount determined by FO for well liabilities on oil and gas lease MTGF 086692.
12/05/2005	MCR LLC	MTB000055 \$25,000 MTB000110 \$35,000	\$60,000 (Increased from \$25,000)	Amount determined by FO for well liabilities
2/01/2006	Macum Energy, Inc.	MT0994	\$100,000 (Increased from \$25,000)	By 1/12/06 U.S. District Court Judge Donald W. Molloy Order CV 00-39-GF-DWM